

Via Federal Express

May 9, 2000

Ms. Donna M. Caton  
Chief Clerk  
Illinois Commerce Commission  
527 East Capitol Avenue  
P.O. Box No. 19280  
Springfield, Illinois 62794-9280

Re: I.C.C. Docket No. 00-0007

Dear Ms. Caton:

Enclosed for filing in the above-referenced action please find the original and three (3) copies of the Comments of the City of Chicago. Please return a file-stamped copy of this letter by return mail for our files and to acknowledge receipt of this filing.

Thank you for your cooperation in this matter.

Sincerely,

Conrad R. Reddick  
Special Deputy Corporation Counsel  
City of Chicago Department of Law  
Room 1040  
30 North LaSalle Street  
Chicago, Illinois 60602  
(312) 744-5738

Enclosures

cc: Patrick Foster  
Robert Bishop  
(via e-mail and U.S. Mail)

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

**ILLINOIS COMMERCE COMMISSION)**

**On Its Own Motion )  
Requirements governing the form and )  
content of contract summaries for the )  
neutral fact-finder process for 2000 )  
under Section 16-112(c) of the Public )  
Utilities Act )  
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**ICC Docket No. 00-0007**

**NOTICE OF FILING**

PLEASE TAKE NOTICE THAT on this date I caused to be mailed to Donna Caton, Chief Clerk, Illinois Commerce Commission, 527 East Capitol Avenue, P.O. Box 19280, Springfield, IL 62794-9280, the original and three (3) copies of the **Comments of the City of Chicago** in the above-captioned proceeding.

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CONRAD R. REDDICK  
Special Deputy Corporation Counsel  
30 North LaSalle Street, Suite 1040  
**Chicago, Illinois 60602**  
**(312) 744-5738**

**CERTIFICATE OF SERVICE**

**I, CONRAD REDDICK, an attorney, hereby certify that a copy of the Comments of the City of Chicago** was served upon the parties listed on the attached service list, by e-mail and by first class mail, postage prepaid, in accordance with the updated instructions posted May 5, 2000 on the Commission's Internet site and the Rules of Practice of the Illinois Commerce Commission.

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**SERVICE LIST**  
**ICC Dkt. No. 00-0007**

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

ON)

**On Its Own Motion** )  
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) **ICC Docket No. 00-0007**

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**COMMENTS OF THE CITY OF CHICAGO**

The City of Chicago ("City"), by its attorney, Mara S. Georges, Corporation Counsel, pursuant to the Neutral Fact Finder's ("NFF") Request for Comments issued -- through the Illinois Commerce Commission ("ICC" or "Commission") Staff -- on April 26, 2000, submits these Comments addressing issues arising from the questions posed by the NFF in the above-captioned proceeding.

Introduction.

1. The Problem

The Chairman's Roundtable Report<sup>1</sup> summarized the current difficulties with the NFF market value determination process as follows:

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<sup>1</sup> Report of Chairman's Roundtable Discussions: Re: Implementation of the Electric Service Customer Choice and Rate Relief Act of 1997 ("Chairman's Roundtable Report") issued

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march 30, 2000.

All roundtable participants expressed the overwhelming opinion that the neutral fact finder (NFF) process is badly flawed and is a major impediment to the development of a competitive electric marketplace in Illinois. More than a few participants echoed the sentiment of one roundtable attendee who stated, “We are getting NFF numbers we just don’t believe and which clearly do not reflect market prices.” (emphasis in original) Chairman’s Roundtable Report at 13.

Because the NFF-determined prices are used in the statutorily required purchased power option (“PPO”) tariffs of Illinois utilities imposing transition charges, they have a significant effect on the development of Illinois’ competitive markets. As the Commission’s January 2000 Assessment of Competition<sup>2</sup> reported to the General Assembly:

The PPO is a convenient means by which the customer may save money without actually choosing a new supplier. . . . In the [Commonwealth Edison Company] service area, PPO service has become the preferred choice for a number of customers. Assessment of Competition at 15.

or the year Summer 1999 to Spring 2000 period are widely regarded as being (in comparison to actual market prices) too low in the summer months and too high in the non-summer periods. *See*, Chairman’s Roundtable Report at 18. As a result, there was considerable concern about the possibility that market growth in Illinois would be adversely affected. Specifically, there was concern about potential “re-monopolization” of the electric industry in Illinois. Chairman’s Roundtable Report at 19.

## 2. The Market Index “Solution”

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<sup>2</sup> Assessment of Competition in the Illinois Electric Industry Three Months Following the Initiation of Restructuring, Illinois Commerce Commission, issued January 2000.

Those concerns about “re-monopolization” certainly played a role in the Commission recent approval of an alternative to the NFF process in Docket No. 00-0259 (Commonwealth Edison Company’s PPO-Market Index tariff). Despite expressed misgivings about the minimal time available for scrutiny of the tariff proposal and the difficulty of any needed modifications, the Commission approved Edison’s tariff proposal. That approval came largely because the Commission concluded that “[b]ased on the information presented, the Commission believes it has been shown that [Commonwealth Edison Company’s] proposal would likely perform better in these respects than does the NFF methodology.”

Informally, and in the Commission proceedings considering the Commonwealth Edison Company (“Edison”) PPO-MI proposal, the City has urged the Commission to consider whether improvements to the NFF process could forestall any need for a precipitous leap to reliance on an index for a very thinly traded (and possibly manipulable) market.

Other approaches to improving the determination of PPO market prices may be equally or more desirable. Could clearer direction to the NFF and a plain statement of the objective of the NFF process -- a market price that is to be used as a surrogate power and energy price for DST (retail) customers -- improve the results obtained through the existing process? Do cost and profit levels for bundled services defined by the DST tariffs enable the NFF to make more effective use of bundled service contracts than in prior years? Dkt. No. 00-0259 Comments of the City of Chicago at 8.

The Commission Staff has now presented for comment the current NFF’s questions about the available latitude for such process improvements. This promising initiative follows suggestions by other parties -- participants in Commission sponsored workshops on the NFF contract review

process and in the April 11 and 12, 2000 discussions with the NFF -- that the Commission should take affirmative steps to improve the NFF process.

The NFF Market Value Determination Is Not Ministerial.  
It Requires the Exercise of the NFF's Sound Judgment.

1. The Specific Qualifications Support the NFF's Discretionary Authority

As the Chairman's Roundtable Report noted (at 13),

"The Customer Choice Law provides very specific criteria for the selection of the NFF, as follows:

*The neutral fact-finder shall be a member of a national accounting firm, shall not have served as the neutral fact-finder in the previous year, and shall be selected from a list of candidates provided by a nationally recognized provider of neutral fact-finders that has established rules for maintaining confidentiality."* (quoting 220 ILCS 5/16-112(b)).

not be necessary or rational if the total substance of the NFF process were simple mathematical calculations

that could be left to computer programs. The NFF has a number of duties under the governing statute that require the exercise of considerable judgment in performing the tasks assigned by law.

The qualifications required for selection as a neutral fact-finder provide a foundation for the judgment calls authorized and required by the statute.

2. The Statutory Language Permits the NFF to Improve the Process

While the NFF is assigned a number of specific duties by PUA Section 16-112,<sup>3</sup> the statute's specificity as to what the NFF must do does not extend to how the NFF is to accomplish the task.

At numerous places, the statute calls on the NFF to exercise significant discretion as to matters that directly affect the market values finally determined. For instance, the NFF's principal duty



under that section is to “calculate market values for electric power and energy for each utility.” Section 16-112(d). However, in performing that duty the NFF (exercising judgment) “may determine that a particular value is appropriate for more than one electric utility.” Indeed, the NFF may also decide (in the exercise of its judgment) that the number of contracts is sufficient for multi-year determinations.

Similarly, although the statute directs that the NFF “shall base calculations of the market values for electric energy on the energy prices stated in the contracts,” the NFF retains considerable latitude to assess the usefulness of each contract. In an extraordinary example of the breadth of the NFF’s authority to exercise its judgment to achieve the statutory objectives, the 1999 NFF report states that the NFF eliminated as unsuitable more than 98% of the contract summaries submitted from its calculations. *See*, Chairman’s Roundtable Report at 16.

The most significant point at which the NFF is required to exercise judgment to determine appropriate market values is in the mandate -- repeated at least 3 times in Section 16-112 -- to “take into account the defining characteristics set forth in subsection (c) of this Section.” 220 ILCS 16-112(d), (e), and (f). Those defining characteristics are described by a non-exhaustive selection of examples<sup>4</sup> that includes nature of the power transaction, firm/non-firm power, peak/off-peak, season, length of contracts, and applicable prices.

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<sup>3</sup> 220 ILCS 5/16-112.

<sup>4</sup> The relevant statutory language is “defining characteristics such as the nature of the power transaction (for example, reserve responsibility (firm, non-firm)), . . . .” 220 ILCS 16-

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112(c).

It is this duty to take account of defining characteristics of the transactions used as inputs to a process to determine market values for the direct access customers of Illinois utilities that offers the greatest opportunity to address the most serious criticism of past market values determinations. The most serious problems with the NFF price determinations to date have been that they do not “take account of the defining characteristics” of the contracts reviewed in calculating the market values required by the statute. Past market value determinations have ignored critical defining characteristics.

Past NFF’s have given no consideration to the fact that many contract summaries submitted are for wholesale power and energy, while the NFF is determining a market value applicable only to utilities’ direct access customers -- customers who by law must be retail customers. If the NFF took account of that distinguishing characteristic, it could make adjustments (given appropriate information) that reflect relevant differences between wholesale and retail transactions.

Differences such as the distinctive price-affecting load profiles (size and shape of blocks of power) of wholesale and retail customers need not have a distorting effect on the NFF determined market values.

Any doubt that the NFF has adequate authority to take account of relevant characteristics of submitted contract summaries from the perspective of its duty to calculate a market value for direct access customers should be removed by the language of Section 16-112(e). In that subsection, the NFF is expressly directed that it “shall develop such values as required to represent the different types of market values of electric power.” 220 ILCS 5/16-112(e) (emphasis added).

The ICC May Inform the NFF's Exercise of Judgment Through Its Instructions.

The NFF -- if it is to perform its statutory duties in a diligent manner -- must understand the use and objectives of the market values it is required to produce. The purposes and regulatory context of the NFF-produced market values are essential background for a responsible exercise of the NFF sound judgment.

The statute does not prohibit the Commission from assisting the NFF in that regard. The Commission could respond to specific NFF inquiries, provide the NFF with requested additional information, or make available to the NFF documents from the Commission's files that memorialize the prior deliberations of the Commission and other interested parties on issues the NFF deems pertinent to its process. For example, extended discussions of the issues surrounding the NFF process are contained in the files of various Commission dockets concerning the process or its output. In response to NFF requests, the Commission could provide a list of the transaction characteristics that past submissions to the Commission have identified as relevant (in the view of the filing party) to the NFF's calculation of market values. Similarly, historical information that allows the NFF to compare tariff rates (and underlying costs to the extent needed) with actual market prices over common time periods could allow the NFF to make calculations that avoid possible mistakes by predecessors.

Even if the form of this exercise must await requests from the NFF to avoid any suggestion of improper interference, the essential point for the NFF and the Commission is that it can go forward. The NFF process is not statutorily held static in the form or design defined by the first NFF's exercise of its duties.

The NFF's Questions.

In this section the City offers brief responses to the NFF's questions. These discussions rest on the more extensive discussion above and, thus, do not repeat much of the detail that may properly apply.

1. *Does the Act provide the NFF with the ability to adjust the prices reported in the contract summaries to be more reflective of actual market prices and/or peak and off-peak energy costs at the time the NFF determines market values? If yes, provide proposed mechanisms to do so and cite the provisions of the Act that permit the NFF to do so.*

The NFF has a statutory duty to prepare the most accurate market values it can -- values that reflect actual market prices. In the calculation process the NFF, unavoidably, must exercise considerable judgment. While the Act<sup>5</sup> may not permit raw adjustments to match the NFF's view of what market values ought to be, it does authorize or require the NFF to take account of distinctive characteristics of the transactions reflected in submitted contract summaries that are likely root causes of the divergences between past market value calculations and observed market prices. The NFF must achieve more accurate market values through calculations that take account of all relevant, price-affecting characteristics of the base transactions and of the target market for which prices are being determined. Additional mechanical steps are suggested in the above discussion.

2. *If the NFF is permitted to adjust contract prices reported to be more reflective of actual market prices, what information is required and how may the NFF seek and receive such*

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<sup>5</sup> Public Utilities Act, 220 ILCS 5/1-101 *et seq.*

*information? Cite the provision or provisions of the Act that permit the NFF to seek and receive such information.*

The NFF is permitted to take account of relevant differences in the characteristics of the base contract transactions and the direct access market for which prices are being determined; the NFF is not allowed simply to “adjust” prices arbitrarily to a different level. Information useful in taking account of price-affecting transaction and market characteristics is described in the preceding discussion. Additional information should be requested as deemed necessary by the NFF in the permitted exercise of its judgment to avoid improper interference with the process by the Commission or any other party. Section 16-112(c) is very clear that the statutorily required content of submitted contract summaries is “at a minimum.” Likewise the Commission is expressly authorized to “adopt orders setting forth requirements governing the form and content of [contract] summaries.” 220 ILCS 5/16-112(c). Inquiries or requests from the NFFs are the most reasonable basis for adoption of information requirements that supplement the statutory requirements.

Dated: May 8, 2000

Respectfully submitted,

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